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IN THE

Supreme Court of the United States

October Term 1936; No. 257.

GUY T. HELVERING, Commissioner, Etc., - - Petitioner,

versus

MIDLAND MUTUAL LIFE INSURANCE COMPANY.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

BRIEF FOR MIDLAND MUTUAL LIFE INSURANCE COMPANY.

A mortgagee does not receive any "income from interest," when, at a foreclosure sale, he "bids in" the property for his debt and interest, if the "fair value" of the property is less than the principal debt (exclusive of interest).

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OPINION BELOW: *Midland Mutual Life* v. *Com'r*, 83 F. (2) 629.

JURISDICTIONAL AUTHORITY: Judicial Code, §240(a), as amended by Act of February 13, 1925.

STATUTES INVOLVED: Revenue Act of 1928, §202; 45 Stat. 791, 842.

DATE OF JUDGMENT, etc. May 6, 1936 (R. 19).

NATURE OF THE CASE, RULINGS, etc. The Commissioner determined a $654.84 deficiency tax against the Midland Mutual Life Ins. Co.

The B.T.A. held that where, at a foreclosure sale, a life insurance company "bid in" mortgaged property for an amount equal to the debt *and accrued interest*, such interest became taxable *interest-income, regardless of the "fair market value" of the property foreclosed.*

The C.C.A. (6th) *reversed* the B.T.A.; and held that where the "fair market value" of the foreclosed property was *less* than the principal debt, no interest-income was received by the mortgagee.

Certiorari was granted.

IN THE

Supreme Court of the United States

October Term 1936; No. 257.

GUY T. HELVERING, COMMISSIONER, ETC., *Petitioner,*

vs.

MIDLAND MUTUAL LIFE INSURANCE COMPANY.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

BRIEF FOR MIDLAND MUTUAL LIFE INSURANCE COMPANY.

The only question involved is whether $5,456.99 *past-due and uncollected* mortgage interest became *automatically transmuted* into $5,456.99 taxable *Interest-income* to a *life insurance* company, simply because, on foreclosing the mortgages, it "bid in" the property for the full amount of its debt and $5,456.99 of interest,* although the B.T.A. specifically found that the fair market value of the property was about $9,000 *less* than the principal debt—to say nothing of the interest.

Did such a protective "buying in" of property (not worth the debt) *ipso facto* constitute, for purposes of *life insurance* taxation, *a receipt of the $5,456.99 past due interest?*

That is the question to be decided here.

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*There was actually $15,538.60 unpaid accrued interest due to the Midland Mutual on the foreclosed properties (R. 7); but as the Midland Mutual's "bid" at the foreclosure sale only included $5,456.99 for unpaid interest, the Commissioner assessed the deficiency tax only on account of $5,456.99 interest which he held should have been included in its taxable income.

The Midland Mutual further lost the $10,081.61 balance of unpaid accrued interest; and it could not even "charge off" that part of the loss in any way, as neither the "bad debt," nor the capital "gain" and "loss," provisions of the Revenue Acts apply to *life insurance* companies.

STATEMENT OF THE FACTS.

1. *The foreclosure suits.* The Midland Mutual is a life insurance company which kept its books on a strictly "calendar-year" "cash receipt and disbursement" basis. It never entered any interest payments on its books or records until they were "actually made to and received by" it (R. 13).

In 1930, it foreclosed six long-defaulted mortgages on Ohio and Michigan real estate. It was the only bidder at the judicial sales. It bid such amounts as would enable it "to realize no loss on account of its investment *in case a redemption should be made from the foreclosure sale*"; and it "bid in" the property "without regard to the actual value, but with a view of protecting the investment in case of redemption," as follows (R. 7, 13-14):

Unpaid principal, plus taxes, court costs, attorneys fees, etc., *i. e.*, "Cost basis"	$123,423.57
Unpaid interest	5,456.99
Property "bid in" for	$128,880.56*
The B.T.A. specifically found that the "fair market values of the properties . . . at the dates acquired are" (p. 4, note, *infra*)	$114,500.00
Loss because the "fair market value" of the property was not worth the amount of its "bid," by the amount of	$14,380.56
Additional loss of unpaid accrued interest not even included in the "bid"	10,081.61
Actual loss to the Midland Mutual on the foreclosed properties	**$ 24,462.17**

*A small discrepancy between the correct "bid" prices given in the 60-day deficiency letter (on the basis of which the exact $5,456.99 interest item was determined, R. 4-7) and the "bid" prices erroneously stipulated (R. 14), is ignored in the Government's Brief; and we shall likewise ignore it.

In 1930, the property was conveyed to the Midland Mutual, but, as just shown, it was not worth anything like the amount of the principal debt, to say nothing of the unpaid interest due (R. 10, 11, 13-17; B.T.A.'s ADDITIONAL FINDINGS OF FACT, p. 4, note, *infra*).

2. *The Midland Mutual's treatment of the interest item.* After acquiring title, the Midland Mutual transferred its investment on its books "from the mortgage loan account to the real estate account"; and carried the property on its books as a real estate asset at an amount [$123,423.57] exactly equal to the *principal debt* only (excluding interest), to-wit;

> "the amount of interest [$5,456.99] included in the bid at said foreclosure sales *was not carried* upon the books . . . as a part of the cost of said properties or as an asset of this petitioner [Midland Mutual]. That is to say, the investments, on the books of the petitioner [Midland Mutual] in each of said properties so acquired included only the *unpaid principal* of the loan thereon and disbursements as aforesaid and *did not include the interest* upon said principal." (STIPULATION OF FACTS, R. 13.)

The Midland Mutual did not include the $5,456.99 interest item as an asset in its Annual Statement (Convention Report) for 1930; never entered it on its books or otherwise treated it as income (R. 13-14); and did not include it as "income received from interest" in its 1930 return.

Nevertheless, the Commissioner assessed a $654.84 deficiency tax, on the ground that the Midland Mutual

had received the $5,456.99 "from interest" in 1930, and should have included it as "gross income" in its 1930 return (R. 5).

3. *The decisions below.* The B.T.A. sustained the Commissioner on the authority of the Eighth Circuit case of *Missouri State Life Ins. Co.* v. *Helvering,* 29 B. T.A. 401, 78 F. (2d) 778 (C.C.A. 8th) [R. 8-11].

On appeal, the Sixth Circuit refused to follow the Eighth Circuit's decision in the *Missouri State Life* Case (R. 20); *reversed* the B.T.A. and held that the Midland Mutual did *not* receive $5,456.99 income "from interest" in 1930 (R. 19-22; 83 F. (2d) 629).

Certiorari was granted to solve the conflict in *reasoning* between the Sixth and Eighth Circuits, respectively (R. 22).

In point of fact, the Eighth Circuit did not actually conflict with the Sixth Circuit, because (1) the B.T.A. found that "the fair market values" of the Midland Mutual's properties were in each instance *less* than the unpaid principal, taxes, court costs, etc.,*

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*On October 7, 1936, the B.T.A. rendered a Supplemental Memorandum Opinion, and made "Additional Findings of Fact," in which it found

"The fair market values of the properties which were acquired in said foreclosure proceedings at the dates acquired are as follows; . . .

Mortgage Loan Number and Name of Mortgagor	Fair Market Value
931—Caruso	$ 8,500
1350—Ransom	15,000
1326—Hallam	16,000
1170—Harrington	37,500
1093—Smith	7,500
623—Dalk	30,000"
[Total "fair market values" of foreclosed properties	**$114,500]**

The values so found were, in each instance, *less* than the re-

whereas, on the other hand, (2) at the time of the Missouri State Life's acquisition of title (so far as the Eighth Circuit's opinion discloses) the property may have been worth *a great deal more* than the principal debt and accrued interest—in which event the interest may well be deemed to have been collected in full (p. 30, *infra*).

The same distinction exists in *National Life Ins. Co.* v. *U. S.*, 4 F. Supp. 1000 (Court of Claims) strongly relied on by the Government (pp. 27-28, *infra*).

The Method of Taxing the Income of Life Insurance Companies.*

Since 1921, the "gross income" of all life insurance companies has always been *strictly limited* to only three items, *i. e.*, Interest, Dividends and Rents (Revenue Act of 1928, 45 Stat. 791, 842)†:

"SEC. 202. GROSS INCOME OF LIFE INSURANCE COMPANIES.

(a) In the case of a life insurance company the term 'gross income' means the gross amount of income **received during the taxable year from interest**, dividends and rents."

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spective unpaid principal mortgage debt, taxes, court costs, etc. (exclusive of all interest).

This Additional Finding of Fact required by the C.C.A.'s Opinion of reversal (R. 22) does not appear in the printed Record in this Court, because the B.T.A.'s Finding was made *after* the filing of the petition for *Certiorari*.

*See Appendix, p. 31; *infra*, for an explanation and historical review of the method of taxing the income of life insurance companies.

† §244(a) of the Revenue Acts of 1921 [42 Stat. 227, 261]; 1924 [43 Stat. 253, 289]; 1926 [44 Stat. 9, 47]; §202(a) of the Revenue Acts of 1928 [45 Stat. 791, 842]; 1932 [47 Stat. 169, 224]; 1934 [48 Stat. 680, 731]; 1936 [49 Stat. 1710].

No Regulations have ever been issued on the subject of interest received or realized in cases of mortgage foreclosures.

Beginning with Regulations 69 (issued under the Revenue Act of 1926) and in all Regulations issued under subsequent Revenue Acts,‡ an Article was inserted entitled

"Uncollectible deficiency upon sale of mortgaged or pledged property,"

which provided for (1) the charging off of such uncollectible *deficiency* as a "bad debt" and (2) capital "gains" or "losses" where the mortgagee bought in the mortgaged property upon foreclosure.

As none of the statutory provisions for either "bad debts" or capital "gains" and "losses" apply to *life insurance* companies (and have not applied to them since the passage of the Revenue Act of 1921), the identic Articles [Nos. 153, 193, 23(k)-3] in Regulations 69, 74, 77, 86 and 94 have no application whatever to life insurance companies (*National Life Ins. Co.* v. *U. S.*, 4 F. Supp. 1000, 1012).

Although the Article in question [Art. 193, Reg. 74] is copied in the Appendix to the Government's Brief, it is nowhere else referred to therein; and hence its provisions may be ignored as totally irrelevant to the present *life insurance* company case.

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‡See Reg. 69, Art. 153 (1926); Reg. 74, Art. 193 (1928); Reg. 77, Art. 193 (1932); Reg. 86, Art. 23(k)-3 (1934); Reg. 94, Art. 23(k)-3 (1936).

SUMMARY OF POINTS DISCUSSED.

1. **The fair market value of the property,* at the time the Midland Mutual acquired it, was only $114,500, which was about $9,000 less than the principal debt (exclusive of all interest)** (p. 8, *infra*).

2. **The Midland Mutual did not "receive", *in cash or in property*, the $5,456.99 accrued interest (or any part thereof); and, therefore, the $5,456.99 was not "gross income" under §202, Revenue Act of 1928** (pp. 9-11, *infra*).

3. **The Midland Mutual's $128,880.56 "bid" at the foreclosure sale did not conclusively establish that the fair value was $128,880.56. The fair value was only $114,500 as found by the B.T.A.** (pp. 12-26, *infra*).

4. **A review of the Government's authorities** (pp. 27-29, *infra*).

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*For grammatical convenience, the six properties and the aggregate "fair values" thereof, will sometimes be spoken of in the singular number, as if there were but one property.

FIRST POINT.

The fair market value of the property, at the time the Midland Mutual acquired it, was only $114,500, which was about $9,000 less than the principal debt (exclusive of all interest).

1. The B.T.A. made an express FINDING OF FACT (which was in exact accord with the uncontradicted testimony R. 15-17), that,

> "The **fair market values** of the properties which were acquired in said foreclosure proceedings at the dates acquired" **were $114,500.**

This was an express finding "upon the ultimate question of fact upon which the rights of the parties depend" (*Botany Mills* v. *U. S.*, 278 U. S. 282, 290).*

That *finding of ultimate fact,* based on the uncontradicted testimony, **is not open to review here** (*Botany Mills* v. *U. S., supra; Philips* v. *Com'r,* 283 U. S. 589, 600; *Burnet* v. *Leininger,* 285 U. S. 136, 138-9).

This Court and the various C.C.A. have repeatedly refused to review questions raised by taxpayers, upon the ground that where the B.T.A.'s Findings of Fact were *against* the taxpayer and were supported by *any* substantial evidence, the findings were not reviewable by the Court.

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*In order to foreclose any possibility of the point raised in the *Botany Mills* case, and to present the naked legal question here involved, the B. T. A. embodied its ultimate finding in the very language of Reg. 74, Art. 193 dealing with the value of property bid in by a mortgagee in foreclosure proceedings (although Art. 193 is, in our opinion, not applicable to life insurance companies, p. 6, ***supra***).

As there, so here.

Here, the B.T.A. has found the ultimate fact *in favor of* the taxpayer. Its finding should not be re-examined.

We, therefore, start out with the undisputed **judicially determined fact** that "the fair market values of the properties which were acquired in said foreclosure proceedings at the dates acquired" were only $114,500.

SECOND POINT.

The Midland Mutual did not "receive", *in cash or in property*, the $5,456.99 accrued interest (or any part thereof); and, therefore, the $5,456.99 was not "gross income" in 1930 (or at any time) under §202, Revenue Act of 1928.

1. Neither the mortgagors nor any third party paid any cash whatever to the Midland Mutual on account of either the defaulted debts or Interest. The Midland Mutual certainly *never received* any part of the $5,456.99 Interest, *in cash* from anyone.

2. All that the Midland Mutual received was title to the foreclosed properties; and, as we have just demonstrated (pp. 8-9, *supra*), the "fair market values" of those properties was only $114,500, which was $9,000 *less* than the principal debt alone (exclusive of all Interest).

The Midland Mutual did not, therefore, receive its *full principal* debt even *in property*. It did not re-

ceive a dollar's worth of property on account of its defaulted Interest.

Indeed, as shown at pp. 2, 4, 9, *supra,* the Midland Mutual actually lost nearly $9,000 of its principal [to be exact, $8,923.57], and its entire $15,538.60 *accrued Interest*—an actual $24,462.17 total money loss on its mortgage investment. And yet, the Commissioner held that $5,456.99 "of income [had been] received during the taxable year [1930] from interest"—*a reductio ad absurdum.**

If, immediately upon acquiring title to the properties, the Midland Mutual had sold them, it would have received only $114,500, as that was their "fair market value"; and by very definition, "fair market value" is the sum at which property may be sold "by one who is willing, but not obliged, to sell, and bought by one willing, but not obliged, to buy" (Cf. *Muser* v. *Magone,* 155 U. S. 240, 249). But according to the Commissioner's theory, the Midland Mutual collected its full $123,423.57 principal debt *plus* $5,456.99 of Interest, notwithstanding the fact that if it had sold the properties the day it acquired them, it would have lost, (as it actually did lose) $24,462.17 of its investment!

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*The value of the property acquired at foreclosure must be first applied to the *principal* debt, (including court costs, taxes, insurance, etc., which by the terms of the mortgage constitute additions to principal); and if the value does not exceed such amounts, no interest income is received. If the value exceeds such amounts, the excess value is next applied to pay the interest, and to that extent interest income is received, and is, of course, taxable (*Doyle* v. *Mitchell Bros. Co.,* 247 U. S. 179, 185; *Drier* v. *Helvering,* 72 F. (2d) 76, 77; *John Hancock Mutual Life Ins. Co.,* 10 B.T.A. 736, 739; *American Central Life Ins. Co.,* 30 B.T.A. 1182, 1190(b)).

As no one paid $5,456.99 *cash* to the Midland Mutual, and as no one conveyed to the Midland Mutual any property worth as much as its *principal* debt, *there could not have been* $5,456.99 "income received during the taxable year from interest" (§202 Rev. Act 1928).

No amount of argument can strengthen the bare undisputed facts (1) that during 1930, the Midland Mutual *did not receive any cash* on account of the mortgage principal or interest indebtedness; (2) that it did not receive anything else of any kind whatever, except a conveyance of the mortgaged property, which was worth about $9,000 *less* than the *principal* debt; and, hence, (3) that no part of the property so acquired was applicable to, or was applied towards, the payment of the defaulted Interest.

3. The Midland Mutual did not capitalize any part of the delinquent interest; did not treat it as income in any way; did not, directly or indirectly, carry it as any part of the cost of the properties or as an asset; and did not include such interest as an asset or otherwise, in its annual statement or in its reports to insurance department (R. 13, 20; p. 3, *supra*).*

*The Government relies on cases where the B.T.A. carefully pointed out that the taxpayers had treated the accrued interest as income for all purposes, and had carried the foreclosed properties into their books *as an asset*, at the full amount of the debt *and interest* (*Missouri State Life Case*, 29 B.T.A. at 407, 78 F. (2d) at 780; *National Life Ins. Case*, 4 F. Supp. at 1005; *Reserve Loan Life Case*, 18 B.T.A. at 364; *American Central Life Case*, 30 B.T.A. at 1187, 1190).

In *Manomet Cranberry Co.*, 1 B.T.A. 706; *Ewen MacLennan*, 20 B.T.A. 900; and *Prudential Ins. Co.*, 330 B.T.A. 332, it is not perfectly clear that the properties were carried on the taxpayer's books as an asset, in the amount of the debt *and interest;* but, however that may be, those cases are entirely distinguishable on another ground, in that the property was apparently worth *more* than the price at which it was "bid in"; in which event, of course, the taxpayer did "receive" the interest *in property*. That fact distinguishes the *Midland Mutual* case from all cases heretofore considered.

THIRD POINT.

The Midland Mutual's $128,880.56 "bid" at the foreclosure sale did not *conclusively* establish that the fair value was $128,880.56. The fair value was only $114,500 as found by the B.T.A.

1. *A "bid" price is not conclusive as to "fair value."* In response to the Government's contention that the foreclosure "bids" conclusively established the "fair value" of the property at $128,880.56—a view contrary to the B.T.A.'s latest decision on that subject*; and, that, therefore, the Midland Mutual had "received" *in property* its entire principal debt *with $5,456.99 Interest,* the C.C.A. said (R. 21):

> "There is urged upon us the existence of a *presumption* that at foreclosure sales the bid price *is* the fair market value of the property. Whether so or not, and this we do not decide, certainly *the presumption* by all familiar rules *must disappear* in the face of unchallenged and uncontroverted evidence that the fair value of the property is less. We know neither reason nor authority for such presumption being given *conclusive* effect. If so, foreclosure sales could never be set aside for inadequacy of price, however gross or shocking to the conscience such inadequacy might be."

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*In *La Arcada Bondholders Committee,* 35 B.T.A. (November 17, 1936), a Bondholders Committee was the sole bidder at a foreclosure sale. The B.T.A. said:

> ". . . the *bid* price . . . *is not conclusive* of cost of depreciable property acquired in foreclosure . . ."

The Syllabus reads:

> "1. . . . the cost of a building acquired upon foreclosure by the bondholders after a single conventional bid of one-half the amount of the outstanding bonds *is not conclusively fixed by the bid price* . . ."

That view is sustained by *Ballentyne* v. *Smith,* 205 U. S. 285, where a foreclosure sale was duly advertised, open and public; no fraud, restricted bidding, or lack of buyers shown; and the accepted bid was the highest. Nevertheless, a judicial foreclosure sale was set aside because,

> "the actual value of the property was at least seven times the amount of the bid" (p. 291). [To the same effect, see 35 C. J. 102, note 19; Cf. *Graffam* v. *Burgess,* 117 U. S. 180.]

The Government's contention is thus refuted, because if, as in the *Ballentyne* case, even a stranger's bid is not conclusive as to the property's value, *a fortiori,* a mortgagee's mere formal "bid" to protect himself, is not conclusive (pp. 14-17, *infra*).

The B.T.A. found *as a fact* that the fair value was $114,500.

Which is to prevail—the fact or a supposed conclusive presumption?

2. *The bids of a mortgagee and a third party occupy essentially different relations to the property's "fair value."* The Government has the erroneous view that when a mortgagee "bids in" property at a foreclosure sale, it is identically the same (not only in *legal effect,* but also in *establishing* value) as if a *stranger* had "bid" the same amount and *paid it in cash* to the mortgagee.

The two situations are very different.

This Court recognized that difference when it held that the Frazier-Lemke Act deprived the mortgagee

of "the following property rights" (*Louisville Bank* v. *Radford*, 295 U. S. 555, 594):

> "2. The right to realize upon the security by a judicial public sale . . .
>
> "4. The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale *or by taking the property itself.*"

The italicized words indicate the distinction between the mortgagee (*a*) receiving from a third party the proceeds of a foreclosure sale, or (*b*) *taking the property itself* through a "bid" at the sale.

It has always been the fundamental law in this country and the very essence of a mortgage, that the mortgagee has the right to have the *property devoted to the satisfaction of his debt;* and, if necessary, to have a sale of the mortgaged property, at which the mortgagee can protect himself by bidding in the property.*

In *Louisville Bank* v. *Radford*, 295 U. S. 555, 578-581, 594, there is an admirable exposition of the rights of a mortgagee. In that case, the mortgagee offered to

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*See Wehle, *Railroad Reorganization Under Section 77 of the Bankruptcy Act: New Legislation Suggested* (1934), 44 Yale L. J., 197, 212:

"Under Anglo-American law, since long prior to 1787, the mortgagee on foreclosure sale has had the optional right either to accept the proceeds of a fair competitive sale (if not more than the amount of his claim), or, if the highest bid at such a sale be insufficient to pay the debt, to bid in the property for himself and have the amount of his bid credited on the mortgage debt; in other words (aside from the right to a deficiency judgment), the mortgagee has traditionally had an optional right either to the proceeds of a fair competitive public sale, or to the property itself. As to the right of the mortgagor to have the property for the amount of the debt, this is so generally familiar as to require no exposition here."

pay $9,205.09 in cash for the mortgaged property, and if accepted,

> "all the money paid in in cash would be immediately returned to it in satisfaction of the mortgage indebtedness" (295 U. S., at 577).

The Frazier-Lemke Act attempted to compel the mortgagee to accept (in satisfaction of its debt) $4,445, which was the *appraised* "fair and reasonable value" and "market value" of the property.

This Court held that even the "bankruptcy" power could not take away *a mortgagee's right to the thing pledged;* that despite centuries of efforts to protect necessitous mortgagors (pp. 578-586, 594), there still remained intact the very essence of a mortgage, *i. e.,* the mortgagee's inviolable right either to receive his full debt with interest in cash, or **to take the property itself;** and that

> "To protect his right to full payment **or the mortgaged property,** the mortgagee was allowed to bid at the judicial sale on foreclosure" (p. 580 and elaborate note).

The whole point of the *Radford* case was that no matter what the fair or market value was, the mortgagee had the right to full *cash* payment (with interest) or **to take the property itself.**

So here. The Midland Mutual was unable to collect its debt with interest *in cash.* Consequently, **it took the property;** but the act of taking did not establish, certainly *did not conclusively establish,* what its "fair value" was.

The Government simply ignores the fundamental fact that when a mortgagee "buys in" property, he does not pay in cash *as a stranger does;* neither does he pay his bid with anything that is worth in cash even the amount of the bid—he simply **gets the thing pledged,** through a judicial foreclosure sale, instead of by a strict foreclosure.

The conventional plan of the mortgagee "bidding in" the property, and then paying for it by a credit on his judgment-debt [while unsecured judgment creditors may get nothing, 295 U. S. at p. 588], is merely the necessary judicial machinery by which, instead of the old automatic foreclosure on default, a judicial sale is provided in order to obtain the highest possible price for the debtor's benefit, and, at the same time, to preserve inviolable the creditor's right to a full cash payment of his debt **or to take the property itself** (pp. 579-581, 584; See 35 C. J., p. 53; 42 C. J., p. 208).

A "bid" represents nothing more than the mortgagee's exercise of his immemorial right to protect his interest in the mortgaged property. His "bid" is merely the enforcement of his mortgage lien and it has no conclusive effect as to the actual fair value of the property purchased. A $100,000 mortgage may be foreclosed on property worth $30,000; and when the mortgagee "bids" it in for (say) $50,000, such "bid" does not *conclusively* establish the "fair value" of the property.

The C. C. A. expressed the same idea when it so aptly stated (and answered) the Government's contention as follows (R. 20):

> "The deficiencies were asserted . . . on the ground that a bid at foreclosure sale by the mortgagee *establishes* the market for the particular property sold and is *determinative* as to receipt of income by the mortgagee. This is because the *legal effect* of such sale is said to be the same as though the mortgagee paid the full amount of its bid in cash and then received in cash the full amount of its debt, so that interest is received by it in cash or its equivalent . . .
>
> "Whatever may be the *legal effect* of a foreclosure sale upon the passing of title and the extinguishment of the mortgage debt, the *fact* indisputably remains that when the mortgagee buys in the property *he does not pay cash.* The law permits him to set-off the debt against the obligation created by his bid. **This distinction is vital in determining whether he has received income.** Without possessing the debt the mortgagee would not bid. He is primarily a lender and a purchaser only through necessity. To say that he pays cash and receives cash **is to fly in the face of the realities.** A mortgage lien upon property of a defaulting mortgagor is generally worth no more than the fair value of the security. It is true that the law invests it with the virtue of currency, but only for a limited and definite purpose—the purchase of the mortgaged property. We are unable to see by what alchemy this baser metal is transmuted into gold through the mere formalities of a foreclosure sale."

3. *The "equivalent" or "exchangeable" value argument.* The Government next insists (Brief, pp. 12, 16, 17), that even if the Midland Mutual did not receive $5,456.99 in actual cash (as of course it did not), still it did receive $5,456.99 in one or the other of the following ways:

(*a*) GOVERNMENT'S BRIEF, pp. 17-19: "*Property of an equivalent value* . . . as shown by the taxpayer's voluntary bid at a public sale, that the *property* in question was worth, to the respondent [Midland Mutual] the full amount of its unpaid principal and accrued interest . . . the *property received* may properly . . . be treated as cash to the extent of its *value*" . . . ". . . where, as here, property is received of the equivalent value of a cash payment of the interest, the statute requires that, to such extent, interest be included in the gross income of the recipient."

Thereby, the Government simply re-asserts that a mortgagee's "bid" finally and conclusively establishes the cash value of the property as the amount of the "bid"—a proposition that is refuted, *firstly,* by the B.T.A.'s *finding of fact* that the value was only $114,500, and, *secondly,* by our argument (pp. 12-13, *supra*) that a "bid" is not conclusive as to value (*Ballentyne* v. *Smith*), and that a *mortgagee's* "bid" does not establish "value," even as much as a stranger's bid.

(*b*) GOVERNMENT'S BRIEF, pp. 12, 16: An indefinite "benefit" or "something of exchangeable value" which requires the mortgagor, *if he redeems the property during the redemption period,* to pay both the debt and $5,456.99 interest.

To that we respond;

First; that the "benefit"—if there be a benefit—is not *income;* even if income, it certainly is not "from interest;" and, hence, it is not "income" within §202;

Second; that the alleged "benefit" is, at most, merely the right to compel the mortgagor either to pay the debt with interest, or let the mortgagee take the

property—but the mortgagee already had that inherent right even *before* the sale. Consequently, he did not, by the sale, acquire a *new* "benefit" worth $5,456.99.

Third; what *is* the "something of exchangeable value" which "the taxpayer has received"? "Exchangeable" for *what?* And for *how much?* The Government's Brief is silent on those points.

The C.C.A. aptly said (R. 21):

> "It is said on behalf of the respondent that by bidding the full amount of its debt the mortgagee secured protection against the mortgagor's redemption; that having acquired a *benefit* it should pay the tax regardless of the value of the property. **But a benefit is not necessarily income.** That need not be demonstrated. Here it is clearly not a gain derived from capital, or received or drawn by the taxpayer for its separate use, benefit and disposal.
>
> The property may be redeemed. In that event income is derived to the extent of interest included in the redemption price. Then interest is paid, and likewise received.
>
> But the property may not be redeemed. Is the realization in the one case no more in respect to the creation of income than mere expectation in the other? We think to put the query is to answer it. As was further said in *Eisner* v. *Macomber,* "It becomes essential to distinguish between what is and what is not income . . .; and to apply the distinction, as cases arise, according to truth and substance, without regard to form.' "

To amplify that argument a little, let us consider two separate properties of *equal value,* subject to equal liens, and "bid in" for the same sum.

In one case, the mortgagor redeems; and the mortgagee receives *in cash* the full debt *and interest.*

In the other case, there is no redemption, and the mortgagee owns the property whose "fair value" (as in the first case) is only 80% of the principal debt.

According to the Commissioner, the mortgagee "received" the *full interest* equally in *both* cases. But the C.C.A. said (R. 21);

> "Is the *realization* in the one case no more in respect to the creation of income than mere *expectation* [never realized] in the other?"

4. If, in order to avoid foreclosure expenses, etc., the mortgagor *voluntarily* conveys the property to the mortgagee in full satisfaction of the debt and interest, and the property is worth *less* than the debt, the Commissioner now concedes that no income has been received, and that the mortgagee has not "received" any interest (*Helvering* v. *Missouri State Life Ins. Co.,* 78 F. (2d) 778, 780 [3, 4] reversing the B.T.A.'s decision [29 B.T.A. at p. 408] in favor of the Com'r on that point; Cf. *Prudential Insurance Co.,* 33 B.T.A. at p. 334; *American Central Life Ins. Co.,* 30 B.T.A. at p. 1190 [a]).

Let us assume that life insurance companies "A" and "B" each have a mortgage of $10,000 with $600 accrued interest on lots "X" and "Y", each worth only $7,000.

Company "A" receives a voluntary conveyance of "X" from the mortgagor, and cancels the $10,600 indebtedness. There is no income or interest received by "A" (78 F. (2d) 778 at p. 780 [3, 4].

Company "B" forecloses on lot "Y" at an expense of $300, and "bids" it in for $10,900. Company "B" [$300 *worse off* than Company "A"] must, according to the Commissioner's theory, return $600 as interest received, and pay the tax thereon.

The C.C.A. thus exposed the fallacy in such a situation saying (R. 21):

> "The court in *Helvering* v. *Missouri State Life Insurance Co., supra,* made a distinction between surrender of mortgaged real estate by the mortgagor to the mortgagee and the purchase of the property by the mortgagee under foreclosure. It concluded that a transaction of the first kind produces no income by way of interest to the mortgagee, while one of the latter does. We are unable to grasp the principle which distinguishes them, and we think the differentiation will not withstand analysis. Where the defaulting mortgagor surrenders the mortgaged property in extinguishment of the debt, the mortgagee acquires as against him a clear title. Where the mortgagee buys the property at foreclosure, he does not get clear title, but one still encumbered by the mortgagor's right to redeem. It seems to us anomalous to hold that one who receives *less* derives income, while one who receives *more derives none.* Demonstrating its conclusion that the recipient of the surrendered mortgage derives no income from accrued interest, the court says: 'If the rule were otherwise, a life insurance company, all of the loans of which were in default and which was obliged to take over from its mortgagors mortgaged lands of little value in order to save the expense and delay of foreclosure, would be in the same situation with respect to interest received as though all of its loans were good and the interest had been paid

> in cash.' We fail to see in what better situation is a life insurance company which not only is obliged to take over from its mortgagors lands of little value, but is in addition subjected to the expense and delay of foreclosure. If the illustration is persuasive in the one case, we are unable to see how it can be any less so in the other."

5. This Court is so familiar with the nature of "income," that we need only add that *gain or profit* is the essential idea of "income";[1] and that in determining what constitutes "income", substance and fact rather than form are to be given controlling weight.[2]

Applying those recognized rules, how can it be said that the Midland Mutual had $5,456.99 "income received during the taxable year [1930] from interest" (§202) when it was unable to collect a dollar of interest from the mortgagors; was compelled to pay taxes, court costs, attorneys' fees, insurance, etc.; and finally had to "bid in" the mortgaged premises (which the B.T.A. found were only worth $114,500) as the sole return for a $138,962.17 mortgage investment—a clear loss of $24,462.17? (p. 2, *supra*).

Do not those "actual facts" show that it did not receive $5,456.99 (or any other sum) as interest in 1930 from those mortgage investments?

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[1] *Doyle* v. *Mitchell Bros. Co.*, 247 U. S. at p. 185; *Eisner* v. *Macomber*, 252 U. S. at p. 207; *Goodrich* v. *Edwards*, 255 U. S. at p. 535; *Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. at p. 175.

[2] *Gulf Oil Corp.* v. *Lewellyn*, 248 U. S. at p. 72; *Eisner* v. *Macomber*, 252 U. S. at pp. 211, 213-214; *U. S.* v. *Phellis*, 257 U. S. at pp. 168, 175; *Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. at p. 174; Cf. *Chattanooga Sav. Bank* v. *Brewer*, 9 F. (2d) 982, 988, and *Southern Pac. R. Co.* v. *Muenter*, 260 Fed. 837, 838 (C. C. A. 9th), holding that the *actual facts* must control, regardless of record resolutions or systems of bookkeeping.

The stability of life insurance itself is based upon the assumption that the company will earn *compound interest at the rate assumed* in the calculation of the premium. Hence, as said in Gephart's Principles of Insurance, pp. 43, 46:

> ". . . this interest accumulation is a very important part of the principle upon which the companies operate. It is these interest accumulations which determine in part the premiums to be charged. . . .
>
> "The most important point to understand in connection with the interest accumulations is that it is not a simple interest accumulation, but a compound interest accumulation . . . the science of life insurance is based upon calculations involving mortality statistics and compound interest earnings.*"

The Commissioner's theory that a life insurance company "receives" interest, when, in point of fact, it cannot collect the interest from the mortgagors, and has to take over real estate of a "fair market value"

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*The best explanation of the absolute necessity for a life insurance company to be sure that it collects compound interest at the rate assumed in its calculation of premiums will be found in *Rhine* v. *New York Life* (App. Div.), 289 N. Y. S. 117, 121-123, 125; affirmed Dec. 31, 1936, —— N. Y. ——; *Maddox* v. *Mutual Life*, 193 Ky. 38, 43.

In view of the restricted character of life insurance investments, greatly lowered interest rates, and the vast amount of maturities and redemptions necessitating reinvestment at lower rates, it is practically impossible for life insurance companies now to reinvest those huge sums at more than a fraction of the rate which the companies assumed they would earn when they fixed their premium rates.

Temporarily, the magnitude of old investments maintains the average interest rate at perhaps a little above the rate assumed; but unless interest rates increase, it may not be a great while before the companies fail to earn the rate assumed in the fixing of the premiums, which means disaster when the interest deficit equals whatever saving the company can make in mortality and expenses.

greatly *less* than even the principal of the debt (thereby losing all of its interest), is obviously untenable, because the company could not pay its policy claims with such non-existent purely theoretical interest.

No beneficiary would accept in payment of a death claim, that which the Commissioner insists is "income received from interest"—because it is purely theoretical, and with it no one could purchase food, clothing or housing.

To be concrete: Suppose, in 1930, the Midland Mutual had discharged all of its policy obligations, except a single policy death claim of $128,880.56; and its only remaining asset was this property which it had "bid in" at foreclosure. We must assume that the property had a fair value of $114,500 (for so the B.T.A. found); and that means that the Company could sell the property for $114,500 (and no more), and pay $114,500 upon the policy claim. Where would the beneficiary get the remaining $14,380.56 of the insurance?

Putting aside the $8,923.57 loss of principal, let us center our attention upon the $5,456.99 which the Commissioner insists the Midland Mutual "received from interest" in 1930.

Where is it? It is non-existent for the purpose of paying the beneficiary, who is clamoring for the balance of his insurance. It is only existent for the purpose of being subject to a tax on that, which, in fact, does not exist.

An Illuminating Test.

Life insurance companies are taxed only upon their *investment* income. Capital "gains" and "losses" do not enter into the determination of their taxable income.

Notwithstanding that, however, what is a *capital* "gain" or "loss" for other taxpayers must likewise be a *capital* "gain" or "loss" for a life insurance company; and what is a *capital* "gain" or "loss" for other taxpayers *cannot possibly be income* for a life insurance company.

In other words, *capital* "gains" and "losses" cannot be transmuted into *income* simply because the recipient is a life insurance company.

With this in mind, let us assume the case of two foreclosed mortgages, one held by an ordinary taxpayer and the other held by a life insurance company—in each instance the situation being as follows:

Principal mortgage debt	$10,000.00
Defaulted interest	500.00
Total	$10,500.00
Bid	$10,500.00

"The fair market value of the property" is established by "clear and convincing proof" to be the respective sums hereafter used in the illustrations (Reg. 74, Art. 193).

(1) If the fair market value were $9,500, then the ordinary taxpayer would receive no income, but would

suffer a $500 *capital* loss, which it could deduct (Art. 193).

The life insurance company would likewise sustain a $500 *capital* loss, which it could not deduct because it is a life insurance company; but, according to the Commissioner's theory, the fair value is immaterial, and the life insurance company must return $500 *income.*

Can that which is a *capital loss* to an ordinary taxpayer, be taxable *income* to a life insurance company?

(2) If the fair market value were $10,200, the ordinary taxpayer would receive $200 income, while the life insurance company (according to the Commissioner's theory), would still receive $500 taxable *income*—although, in fact, each company *lost* $300 of interest income.

How can precisely the same situation produce $200 *interest* income to an ordinary taxpayer, and $500 *interest* income to a life insurance company?

(3) If the fair market value were $10,700, then the ordinary taxpayer would receive $500 interest income and $200 capital gain, while the life insurance company (according to the Commissioner's theory) would receive $500 interest income; and although actually realizing a $200 capital gain, it would not have to account for it for two reasons: (*a*) Capital "gain" provisions do not apply to life insurance companies, and (*b*) The $10,500 bid is *conclusive* of the fair value, regardless of the actual facts!

FOURTH POINT.

A review of the Government's authorities.

As the Government's argument consists principally of a quotation from the *Missouri State Life* case (C.C.A. 8th), and nearly four pages (Brief, pp. 10-11, 13-15), taken literally from the Court of Claims' opinion in *National Life Ins. Co.* v. *U. S.*, 4 F. Supp. 1000, a review of those two cases is all that is necessary.*

In *National Life Ins. Co.* v. *U. S.*, 4 F. Supp. 1000, a life insurance company foreclosed a number of mortgages in States where there were redemption laws. The Company (as the only bidder at the foreclosure sales) bid the full amount of the unpaid principal and accrued interest. The Company carried the purchased real estate as an asset to the value of the debt and interest; and included the interest as income in its annual statements to the Insurance Departments of the various States, as well as including it as income in its Federal Income Tax Returns. Later it sued for a refund of the tax on such interest.

The Court of Claims found that, at the date of foreclosure, some of the property had a "fair market

*The other cases cited are (1) the B.T.A.'s previous rulings on the same subject (Brief, pp. 8-9; reviewed p. 11, note, *supra*); (2) those cited in the *National Life* opinion (which with scarcely a changed word constitutes the Government's argument in its Brief, pp. 13-15); (3) *American Cigar Co.* v. *Com'r*, 66 F. (2d) 425, which was not a foreclosure case, but was a "bad debt" case, involving a loan to a debtor, *whereas* the "bad debt" provision does not apply to life insurance companies, and there was no loan here to the debtor; and *Duke Power Co.* v. *Com'r*, 44 F. (2d) 543, which was not a foreclosure case, but involved the right to file consolidated returns of affiliates.

value" equal to the debt and interest; and that some of the other purchased real estate was later sold for *more* than the debt and interest.

The opinion does not show that any of the purchased real estate had a "fair value" of *less* than the debt and interest; so that, as far as the opinion reveals, *all* of the purchased real estate may have had an actual "fair value" *more than* the debt and interest. If so, the National Life certainly realized either interest-income or a capital "gain"—in either instance a totally different situation from that presented in the Midland Mutual's case.

This difference between the facts in the *National Life* and *Midland Mutual* cases, respectively, not only prevents the *National Life* case from being an authority in the *Midland Mutual* case, but greatly lessens the value of its general reasoning as applied to the very different facts here involved.

In brief, the Court of Claims simply holds that when the National Life bid the amount of the debt and interest at the foreclosure sale, so as to obtain title free from the redemption laws, the transaction was exactly the same as if a stranger had bid the same sum, had paid it into Court, and the mortgagee had collected it in cash, in which event the mortgagee would have received the interest as taxable income.

It is useless to lengthen this Brief by considering separately the arguments taken from the *National Life* opinion, as the substance of each of them has already been thoroughly considered, analyzed and answered (pp. 9-26, *supra*).

In *Helvering* v. *Missouri State Life Ins. Co.*, 78 F. (2d) 778 (C.C.A. 8th), a life insurance company acquired mortgaged property in two ways: (1) at foreclosure sales, by "bidding" it in for the full amount of the principal debt with interest, and (2) by voluntary conveyances from the mortgagor, in consideration of the forgiveness of the entire indebtedness.*

With respect to mortgage foreclosures, the C.C.A. held that where the "bid" was equal to the principal debt with interest, the mortgagee had received the interest, regardless of whether the bid was by the mortgagee or by a stranger, disposing of the matter in the following summary fashion;

> "When mortgaged property is sold on foreclosure for an amount sufficient to pay the mortgage debt with accrued interest, the mortgagee has received payment in full of its debt, and that is so, regardless of whether the highest bidder at the sale is the mortgagee or a stranger. Where a stranger buys, he pays cash to the officer making the sale, who pays it to the mortgagee. Where the mortgagee buys the property, instead of paying cash to the officer and receiving it back, he credits the amount which he, as purchaser, bids, upon the mortgage debt. In either event, he receives payment in cash or its full equivalent." [Citation omitted.]

This argument has been fully answered at pp. 13-17, *supra*.

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*The C.C.A. (8th) held that in the cases of voluntary conveyance, if the land was worth as much as or more than the debt with interest, the Company had received the interest income; but if the property was worth *less* than the principal debt, no interest was received.

As there were no findings as to the "fair value" of the properties voluntarily conveyed, the case was remanded on that point.

The *Missouri State Life* case is not really in point, because, so far as the 8th Circuit's opinion discloses, the "fair value" of the foreclosed property may have been a *great deal more than* the entire principal debt, costs, *and all accrued interest,* in which event it would present an entirely different situation from that of the Midland Mutual, where the B.T.A. has found that the "fair value" of the property was actually *less* than the principal debt alone.

If we turn back to the B.T.A's opinion in the *Missouri State Life* case (29 B.T.A., pp. 407-408), it appears that there was much testimony in the record upon the question of the "fair market values"; but the B.T.A. (thinking that point immaterial), made no express findings on the subject, except to say that the fair market values of *some* of the properties were less than the loan, *plus* accrued interest. From the context, it would seem that it referred to properties where *voluntary conveyances* had been made. However that may be, in any event most of the foreclosed properties may have had a "fair value" greatly in *excess* of the principal debt *and all interest thereon.*

The great difference between the clear, undisputed facts in the *Midland Mutual* case and the very different facts in the *National Life* and *Missouri State Life* cases prevents the latter from being a direct authority.

CONCLUSION.

The judgment should be affirmed.

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Counsel for Respondent.

4 January 1937,
Louisville, Ky.

[See pages 32-34, *infra*, for Appendix.]

APPENDIX.

METHOD OF TAXING THE INCOME OF LIFE INSURANCE COMPANIES FROM 1913 TO 1936.

In view of the Government's repeated reference to, and reliance upon, the fact that life insurance companies are not subject to the capital "gains" and "losses" provision of the income tax law; its insistence that they have received "privileged treatment . . . different from that of other corporations and individuals"; and the erroneous inferences drawn therefrom (Government Brief, pp. 7, 15, 19), the following review is submitted:

1913-1920. The Revenue Acts of 1913, 1916, 1917 and 1918, taxed life insurance companies upon their *net income;* and all *premiums* paid in by policyholders were included as "*gross* income." On account of the peculiar nature of the life insurance business, Congress allowed certain large *special deductions,* summarized in the margin,* in order to exclude from "*net*" income the enormous sums which the companies (1) paid out to policyholders, or (2) were compelled to retain as legal "Reserve" to meet future death losses as they should occur (*Maryland Casualty Co.* v. *U. S.,* 251 U. S. 342, 346-8; BRANDEIS, J. dissenting in *National Life Ins. Co.* v. *U. S.,* 277 U. S. 508, 522-523; *Helvering* v. *Ind. Life Ins. Co.,* 292 U. S. 371, 379; *Rockford Life Ins. Co.* v. *Comr.,* 292 U. S. 382, 383, 385).

*The special deductions so allowed (1913-1920) were, to wit; (1) the net addition required by law to be made within the taxable year to Reserve funds; (2) sums other than dividends paid within the taxable year on policy and annuity contracts; and (3) in the 1918 Revenue Act, such portion of any actual premium received from any individual policyholder as is paid back or credited to, or treated as, an abatement of premium of such policyholder within the taxable year (Act Oct. 3, 1913, Section II G(b), 38 Stat. 172-3; Revenue Act of 1916, § 12(a), 39 Stat. 767-8; Revenue Act of 1917, 40 Stat. 302-305; Revenue Act of 1918, §§ 233(a)(1), 234(a)10, 40 Stat. 1077, 1079; Compare Act August 5, 1909, § 38, 36 Stat. 113).

This was so, on exactly the same theory that if Congress includes in a bank's income *all the money deposited in the bank by its depositors during the year,* it must either (*a*) make the tax infinitesimally small or (*b*) allow as a *deduction,* all the checks drawn by depositors during the year *plus* the amount owing to depositors at the end of the year.† In the *National Life* case Solicitor General MITCHELL expressly so conceded, aptly saying that *premiums*

> "*are no more income to the company* than are *deposits* in a bank *income to the bank*" (Brief, p. 12).

Otherwise, both the banking and insurance businesses would be taxed out of existence.

That treatment of premiums as "income," with corresponding special deductions, was productive of administrative difficulties and much litigation (*McCoach* v. *Insurance Co.,* 244 U. S. 585; *Maryland Cas. Co.* v. *U. S.,* 251 U. S. 342; *U. S.* v. *Boston Ins. Co.,* 269 U. S. 197; *New York Life Ins. Co.* v. *Edwards,* 271 U. S. 109; *Duffy* v. *Mutual Benefit Co.,* 272 U. S. 613 BRANDEIS, J., in *National Life Case,* 277 U. S. at 523; *Helvering* v. *Ind. Life Ins. Co.,* 292 U. S. 371, 379).

1921-1936. The 1921 Revenue Act simplified the taxation of life insurance companies by adopting a new method, which has been followed in all the subsequent Revenue Acts of 1924, 1926, 1928, 1932, 1934 and 1936 (p. 5, note, *supra*). This new method was not an arbitrary favor or "privileged treatment" [as the Government asserts, Brief, p. 19]; but, as Mr. Justice Brandeis (dissenting) said in *Nat'l. Life Ins. Co.* v. *U. S.,* 277 U. S. 508, 535,

†Cf. *Deposit Bank of Owensboro* v. *Daviess County,* 102 Ky. 174 at 214; *Com.* v. *Bank of Commerce,* 118 Ky. 547, 551-556; *Com.* v. *Wathen,* 126 Ky. 573, 574; *Branch* v. *Town of Marengo,* 43 Ia. 600; *People* v. *Peck,* 157 N. Y. 51; *In re Haight,* 32 App. Div. 496; *State* v. *Carson Savings Bank,* 17 Nev. 146; *State* v. *American,* 37 N. J. Law, 408; *Petition of Savings Bank,* 68 N. H. 384; *Berry* v. *Windham,* 59 N. H. 288; *Clement Nat. Bank* v. *Vermont,* 231 U. S. 120.

> "The new method of taxation was intended by Congress to procure *additional revenue* from the insurance companies." House Report 67th Congress, 1st Session, No. 350, p. 14."

The new method *eliminated premiums* from "gross income," by defining "gross income" to include *only* such income as was "*received* during the taxable year" from "*interest, dividends and rents*" [§244(a)].

On the other hand, it *eliminated* many *deductions* which *other* corporations were allowed [Cf. §§234(a), 245(a)].*

The new 1921 method (which is still in force after sixteen years) was not some "privileged treatment" which the companies secured as a favor from Congress. It was the result of several years' careful consideration by the Treasury Department and by Congressional Committees in an effort *to collect more taxes* from life insurance companies than had been possible under the previous Revenue Acts taxing life insurance companies and allowing them capital "gains" and "losses," etc., like other corporations (Cf. §§246(a)(1)(2), 247 of Senate Amendment to Revenue Act of 1918 (Senate Report No. 617, 65th Cong. 3d Sess. H. R. 12863); Hearings before the Senate Committee on Finance, on H. R. 8245, 67th Cong., 1st Sess., p. 84, September 1-October 1, 1921. See also S. Rep. No. 275, 67th Cong., 1st Sess., p. 20; §§244(a), 245(a)(1)(2) Revenue Act of 1921, 42 Stat. 261. Cf. BRANDEIS, J., in *National Life* case, 277 U. S. at 523 note; *Helvering v. Ind. Life Ins. Co.*, 292 U. S. 371, 379; *Rockford Life Ins. Co. v. Comm'r*, 292 U. S. 382, 385).

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*In lieu of the former (1913-1920) special deductions noted in the margin (p. 31, *supra*), the 1921 Act allowed *only nine deductions* specifically itemized in the nine separate numbered paragraphs of §245 a), (1) to (9).

These deductions were not an arbitrary favor or "privileged treatment," but were an *economic necessity*, so long as there was any pretense of "income" taxation; though, constitutionally, Congress might have refused any deduction, and taxed the life insurance business into insolvency.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 257.

GUY T. HELVERING, Commissioner, Etc., - Petitioner,

versus

MIDLAND MUTUAL LIFE INSURANCE COMPANY, - - - - - - Respondent.

PETITION FOR A MODIFICATION OF THE OPINION.

F. J. WRIGHT,
JOHN E. TARRANT,
WM. MARSHALL BULLITT,
Counsel for Midland Mutual Life Insurance Company.

WESTERFIELD-BONTE COMPANY, INCORPORATED, LOUISVILLE, KY.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 257.

GUY T. HELVERING, COMMISSIONER, ETC., - *Petitioner,*

v.

MIDLAND MUTUAL LIFE INSURANCE COMPANY, - - - - - - - *Respondent.*

PETITION FOR A MODIFICATION OF THE OPINION.

Midland Mutual petitions for a modification of the opinion because of its statement:

> "We cannot say that Congress did not intend to include in its definition [*i. e.*, of the gross income of life insurance companies] a case like the present merely because the taxpayer *received a credit rather than money or other tangible property.*"

We suggest that Congress did not intend a foreclosure bid to be the criterion for determining income, gain or loss; but intended the criterion to be the "*fair market value of the property*" *bought in.*